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No. 81-2126

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

T.H. BELL, SECRETARY OF EDUCATION,
Petitioner,
v.
STATE OF NEW JERSEY

T.H. BELL, SECRETARY OF EDUCATION,
Petitioner,
v.
COMMONWEALTH OF PENNSYLVANIA

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

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BRIEF FOR *AMICI CURIAE* NATIONAL ASSOCIATION OF COUNTIES; NATIONAL LEAGUE OF CITIES; UNITED STATES CONFERENCE OF MAYORS; AMERICAN PUBLIC WELFARE ASSOCIATION; NATIONAL COUNCIL OF LOCAL PUBLIC WELFARE ADMINISTRATORS; CITY OF STOCKTON, CALIFORNIA; CITY AND COUNTY OF LOS ANGELES, CALIFORNIA; COUNTY OF ONSLOW, NORTH CAROLINA; CITY OF PORTLAND, OREGON; CITY AND COUNTY OF SAN FRANCISCO, CALIFORNIA; CITY OF BOSTON, MASSACHUSETTS; BROWARD EMPLOYMENT AND TRAINING ADMINISTRATION; STATE OF MAINE; STATE OF NORTH CAROLINA; CITY OF SEATTLE, WASHINGTON; ALAMEDA COUNTY TRAINING AND EMPLOYMENT BOARD, CITY OF SAN JOSE, CALIFORNIA; STATE OF VERMONT; COUNTY OF CUMBERLAND, NORTH CAROLINA; CITY OF MEMPHIS, TENNESSEE; CITY OF DETROIT, MICHIGAN; CITY OF BRIDGEPORT, CONNECTICUT; CITY OF CAMDEN, NEW JERSEY; TOLEDO AREA CETA CONSORTIUM, OHIO; STATE OF OHIO; AND GENESEE-LAPEER-SHIAWASSEE-FLINT, MICHIGAN, CONSORTIUM

[Attorneys Listed on Inside Cover]

Wilson - Epes Printing Co., Inc. - (202) 789-0096 - Washington, D.C. 20001

ROBERT N. SAYLER *
JOHN E. HEINTZ
KAREN H. ROTHENBERG
JOAN E. DONOGHUE

COVINGTON & BURLING
1201 Pennsylvania Avenue, N.W.
P.O. Box 7566
Washington, D.C. 20044
(202) 662-6000

Attorneys for Amici Curiae

* *Counsel of Record*

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BRIEF FOR *AMICI CURIAE*

INTRODUCTORY STATEMENT

This case raises an issue of great significance to all state and local governments that participate in joint programs with the federal government. The Department of Education (the "Department"), the federal partner in the elementary and secondary education assistance program, seeks to require its state partners to repay, dollar-for-dollar, funds found to have been misspent by the non-federal partners many years ago. The Department seeks to impose this retroactive repayment sanction regardless of the gravity of the state partners' mistakes and despite the federal government's failure to warn prospective grant recipients that they, and not the federal government, would bear sole responsibility for mistakes and would be subject to retroactive fiscal sanctions. It is obvious from the government's brief that if it prevails

here, it will seek to apply this notion to numerous other grant programs without regard to statutory language or the history of the program.

The government has seriously misconceived the nature of this case. Throughout its brief, it suggests that all grantees subject to audit disallowances are guilty of intentionally diverting federal funds to their own purposes or, at best, of misconduct by which they would be unjustly enriched if allowed to retain misspent funds. The government's gross mischaracterization leads it to conclude that it is not unfair to recoup misspent funds from such grantees, and indeed that justice compels recoupment.

This case, however, like most cases, does not involve bad conduct. Rather, it involves two state governments that, in discharging in good faith their responsibilities to implement and administer a large, complex federal program under an intricate set of rules and regulations, allegedly made mistakes. The states did not divert federal monies to their own purposes. They did not use the funds they received to save state funds they otherwise would have spent or to support other services that otherwise would have been financed by state funds. Like most state and local grant recipients, they simply expended the grant funds they received for activities that, at the time, both they and federal officials believed served the objectives of the Congress. The funds are gone. Now, many years later, the federal government seeks return of a portion of those funds because its auditors concluded that the states had not spent the funds precisely as intended. Such an action only serves to punish the grant recipient while absolving the federal partner of all responsibility for mistakes made in carrying out the program and while enhancing the federal treasury. If the states were required to repay disallowed costs, the intended beneficiaries of the grant would not benefit. The only beneficiary would be the federal fisc at the expense of the taxpayers of the two states.

There is no doubt that the illegal or fraudulent use of grant funds may be redressed under the criminal laws. Moreover, Congress clearly has the power to redress the knowing misuse of funds and a federal agency has the power closely to supervise the expenditure of funds it disburses to grantees. We do not challenge Congress' power to redress good faith mistakes made by grantees when implementing complex federal programs by authorizing federal agencies to impose such sanctions. We proffer but one basic principle: The federal government cannot require a state or local government grantee to repay federal grant monies from non-federal sources where as here the grantee was found to have misspent funds in a good faith effort to implement the grant, unless the federal government has given advance notice—by statute and regulations—to all prospective grantees of its intention to require such repayment.

Congress did not give state and local governments such advance notice under the Elementary and Secondary Education Act ("ESEA"). Absent such authorization a federal agency cannot require repayment from non-federal sources. Similarly, the Department did not give advance notice that repayment from non-grant sources would be required by promulgating regulations. Assuming *arguendo* that an agency may validly provide by regulation that grantees found to have misspent funds will be required to repay such funds from non-grant sources in the absence of statutory authority, a point we do not concede, the Department did not attempt to do so here.

Like ESEA, the Comprehensive Employment and Training Act ("CETA") of 1973, in which most Amici participated, did not include repayment among the noncompliance sanctions available to the Department of Labor. In 1978, Congress amended both ESEA and CETA to provide for such a repayment sanction. In neither case may the administrative agencies apply these provisions retroactively to disallowed grant funds received prior to the 1978 amendments. Moreover, the Depart-

ment of Labor, like the Department of Education, failed to provide for such a repayment sanction in its regulations. Therefore, state and local governments that received CETA funds prior to the effective date of the 1978 Amendments, like their counterparts under ESEA, may not now be required to repay those funds out of non-grant monies.

The principle that a federal agency may not impose a fiscal sanction without Congressional authorization does not mean that state and local governments may disregard federal requirements with impunity when expending federal grant funds. The federal government must, however, explicitly and unambiguously inform state and local governments of the consequences of their failure to conform fully to federal requirements. The federal government may not claim, *post hoc*, that authority to impose fiscal sanctions can be implied *sub silentio*.

Congress carefully chooses the types of sanctions that it determines are appropriate for a particular program. In the case of both ESEA and CETA, Congress initially authorized the imposition of only certain limited sanctions, from which repayment was omitted. Neither agency sought to implement a repayment sanction by regulation. Congress later expanded the authority of both agencies to include the repayment sanctions urged here. Subsequently, Congress cut back on that authority when enacting block grant legislation in 1981 and 1982. All that can be deduced from the Congressional omission of a repayment sanction in the original ESEA and CETA legislation is a decision not to authorize the imposition of fiscal repayment sanctions. Where Congress has not included a repayment sanction among the sanctions it authorizes an agency to impose on its state and local government partners, the agency cannot impose such a sanction outside the authority granted it. Moreover, any authority that was granted and later revoked cannot be applied retroactively.

INTEREST OF *AMICI CURIAE*

This case has potential significance for every state and local government that has received federal grants over the last decade. While there are differences in the statutes authorizing these programs that may bear on the government's power to impose fiscal sanctions of the sort urged here, there is no doubt that the government seeks to establish a rule that it would apply to all grant programs. At present, many millions of dollars currently are in dispute at various stages of audit and disallowance proceedings under the Comprehensive Employment and Training Act ("CETA") program alone.[1] In those proceedings state and local government participants in CETA ("prime sponsors") maintain or may maintain that the Department of Labor does not have the authority to request repayment of allegedly misspent CETA funds disbursed prior to the implementation of the 1978 CETA Amendments from non-grant sources.

Each of the Amici are or were prime sponsors, served as prime sponsors within consortia of city, county, or state sponsored CETA programs, or represent the interest of local and state governmental agencies whose resources will be further drained if required to repay allegedly misspent CETA funds from non-CETA sources.

1. *The National Association of Counties (NACO)*: This membership organization represents the interests of approximately 2,100 counties throughout the United States. Counties, directly and through their membership in consortia, constitute over seventy percent of the over 475 CETA prime sponsors nationwide.

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[1] Based on reports issued by the Department of Labor, it appears that audit resolution activity for the last two semiannual periods alone totalled disallowed costs for state and local prime sponsors of some $62 million. Other grantees and subgrantees were disallowed some additional $39 million. *See*, U.S. Department of Labor, Semiannual Report of the Inspector General, April 1, 1981—September 30, 1981, Appendix at 114 and U.S. Department of Labor, Semiannual Report of the Inspector General, October 1, 1981—March 31, 1981, Appendix at 78-79.

2. *The National League of Cities (NLC)*: This non-profit membership organization assists municipalities in performing their functions. Its membership includes direct member cities, state leagues of municipalities and state league member cities, many of which have served as prime sponsors under CETA. In all, almost 15,000 cities and municipalities are members of and participate in the actvities of NLC. The functions of NLC as authorized in its Bylaws include "the safeguarding of the interests, rights, and privileges of municipalities."

3. *The United States Conference of Mayors*: The Conference is an organization of city governments represented through their chief elected officials, Mayors. The Conference was organized to promote the causes of cities and to foster responsible and effective relationships between city halls and the federal government. The Conference represents cities of over 30,000 in population, including virtually all cities of over 100,000, most of which have served as prime sponsors under CETA. The Conference operates a clearinghouse on a fee basis for over 120 prime sponsors and has been involved actively in the development and review of CETA statutes and regulations.

4. *American Public Welfare Association (APWA)*: This non-profit membership organization is concerned with the effective administration and delivery of all human service programs. Members include virtually all state and territorial public agencies, more than 1,200 local governments and non-profit agencies, and some 6,500 individuals. The APWA has a vital interest in the federal-state-local partnership for sound and effective administration of human service programs, including CETA.

5. *National Council of Local Public Welfare Administrators*: This affiliate of the APWA represents approximately 150 administrators of local public welfare programs. Although many county welfare departments do not directly sponsor CETA programs, they have a vital interest in maintaining the integrity of employment programs.

6. *City of Stockton, California*: The City participates in the Stockton/San Joaquin Consortium, a CETA prime sponsor. The City is presently challenging the disallowance of hundreds of thousands of dollars before the Department of Labor, in part for periods prior to implementation of the 1978 CETA Amendments.

7. *The County of Los Angeles, California*: The County participates in a consortium which serves as a CETA prime sponsor. It is challenging the disallowance of millions of dollars, in part for CETA funds disbursed for periods prior to implementation of the 1978 Amendments.

8. *City of Los Angeles, California*: The City of Los Angeles has served as a CETA prime sponsor and is subject to audit disallowances of some $180,000 for periods prior to the 1978 CETA Amendments.

9. *County of Onslow, North Carolina*: Onslow County served as a CETA prime sponsor for the years 1974-78. It is presently challenging hundreds of thousands of dollars proposed for disallowance.

10. *City of Portland, Oregon*: The City of Portland's Training and Employment Division serves as a CETA prime sponsor. The City is presently challenging the disallowance of approximately $1 million, most of which is for periods prior to implementation of the 1978 CETA Amendments.

11. *City and County of San Francisco, California*: The City and County serves as a CETA prime sponsor and is challenging an audit finding that it earned and is required to refund over $200,000 in interest on CETA funds held prior to disbursement for program purposes, in part for periods prior to implementation of the 1978 Amendments.

12. *City of Boston, Massachusetts*: The City of Boston has served as a prime sponsor for CETA grant programs since 1973. The City is presently challenging the disallowance of approximately $1.6 million, all for periods

prior to the implementation of the 1978 CETA Amendments.

13. *The Broward Employment and Training Administration (BETA)*: This consortium serves as a prime sponsor for Broward County, Florida, and the Cities of Ft. Lauderdale and Hollywood, Florida. It is presently challenging the disallowance of millions of dollars, in part for CETA funds disbursed for the periods prior to implementation of the 1978 Amendments.

14. *State of Maine by its Attorney General*: The State of Maine, through the Office of Maine CETA, has served as a CETA prime sponsor since CETA's inception. It is presently challenging the disallowance of several hundred thousand dollars of funds received and disbursed prior to the implementaton of the 1978 CETA Amendments.

15. *State of North Carolina*: The State serves as a CETA "balance of state" prime sponsor. The State is presently challenging the disallowance of approximately $100,000 in the Court of Appeals for the Fourth Circuit, all of which is for periods prior to the implementation of the 1978 CETA Amendments.

16. *City of Seattle, Washington*: The City is part of the Employment and Training Consortium which is the CETA prime sponsor for the Seattle/King County area. The Consortium is challenging questioned costs of hundreds of thousands of dollars, all of which is for periods prior to implementation of the 1978 CETA Amendments.

17. *Alameda County Training and Employment Board*: The Board is a consortium prime sponsor consisting of 13 local governments, one of which is the County of Alameda, California. The rest include the cities of Alameda County, with the exception of Oakland and Berkeley. The Board is engaged in administrative proceedings involving several hundred thousand dollars.

18. *City of San Jose, California*: The City served with the County of Santa Clara as a CETA prime spon-

sor until late 1980. The City is challenging the disallowances of millions of dollars, a large part for the period prior to implementation of the 1978 Amendments.

19. *State of Vermont*: The State serves as a CETA "balance of state" prime sponsor. The State is challenging thousands of dollars of disallowed costs, most for periods prior to implementation of the 1978 Amendments.

20. *County of Cumberland, North Carolina*: Cumberland was a prime sponsor during the period prior to implementation of the 1978 Amendments and is currently contesting some $100,000 of proposed disallowances.

21. *City of Memphis, Tennessee*: As other prime sponsors, the City of Memphis is facing challenges to pre-1978 expenditures under the CETA program.

22. *City of Detroit, Michigan*: The City of Detroit is a prime sponsor of CETA grant programs; it has received audit exceptions from the Department of Labor for an amount in excess of $8,000,000.

23. *City of Bridgeport, Connecticut*: The City of Bridgeport has served as a prime sponsor for CETA grant programs since the inception of the CETA program. The City is facing audit exceptions for more than $500,000 for the period prior to Fiscal Year 1978.

24. *City of Camden, New Jersey*: The City of Camden has been a prime sponsor since 1973. The City is concerned about the drain on local general revenues that a use of a recoupment procedure would have.

25. *Toledo Area CETA Consortium*: This Consortium is the CETA prime sponsor for Lucas and Wood Counties and the City of Toledo, Ohio. Repayment of approximately $3,000 for audit exceptions for pre-1978 efforts has been made by the Consortium from the general revenue funds of the City of Toledo.

26. *State of Ohio*: The Office of Manpower Development of the Ohio Bureau of Employment Services serves as CETA Balance of State Prime Sponsor for the

State of Ohio. The Office of Special Grants of the Ohio Bureau of Employment Services administered CETA Special Grants to Governors. Audits of both agencies have questioned or are anticipated to question between $150 million and $200 million under grants issued prior to the 1978 CETA Amendments.

27. *Genessee-Lapeer-Shiawassee-Flint (GLSF) Employment and Training Consortium*: The GLSF Consortium was founded in 1974 at the time that CETA grants were first implemented. The Consortium includes three counties and one city in the state of Michigan. The Consortium is facing thousands of dollars in disallowed costs for the period prior to 1978.

SUMMARY OF ARGUMENT

Amici submit that the government's position is flawed for the following reasons:

First, the pre-1978 Education Act, in place at the time of the alleged misspending, prescribed certain remedies and sanctions but the one employed here—retroactive imposition of fiscal sanctions—was not among them. The Department's regulations failed to set forth the sanction sought here. Both the statute and regulations serve as a bar to creation and imposition of different and unprescribed remedies.

Second, the 1978 Education Amendments *did not* authorize imposition of retroactive fiscal sanctions. Far from conferring the power to read those sanctions into the pre-1978 statute, the new provision confirms that this power was not in place at an earlier time. The 1978 Amendments were not made retroactive. Further, the statute cannot be given retroactive effect in view of the Department's regulations. Retroactive application would trample upon the well-established administrative law principle that affected parties are entitled to rely upon regulations in place at the time requested activity takes place. Moreover, under the Administrative Procedure Act

even the prospective application of the 1978 Amendments is improper unless properly implemented by regulation.

Third, retroactive sanctions, if unauthorized by statute and regulations, cannot be founded on the common law. The statute deals with the matter of sanctions; Congress could not have intended *sub silentio* to invest the Department with other unspecified sanction powers and the Department's regulations block the arrogation to the Department of any common law powers. In any case, the present proceeding is not a common law recoupment action but a review of an administrative decision to consider the legality of sanctions imposed "under" the statutory sanction provisions of the Act.

ARGUMENT

I. THE DEPARTMENT OF EDUCATION DID NOT HAVE AUTHORITY TO REQUIRE REPAYMENT OF MISSPENT TITLE I FUNDS FROM NON-GRANT SOURCES DURING THE YEARS AT ISSUE.

Prior to 1978, the Act provided no legal basis for the action taken by the Department in this case. The Act contained no express authority that would permit the Department to require repayment of misspent Title I funds from non-grant sources nor did Congress intend to give the Department such authority. Moreover, such authority cannot be implied. Finally, even if the Act contained such authority, explicitly or implicitly, the Secretary cannot exercise that authority because he failed to implement it by promulgating regulations as required by the Administrative Procedure Act, 5 U.S.C. § 553. The first two of these points is discussed below; the last point is discussed in Section III, *infra*.

A. Prior to 1978, the Act did not authorize a repayment sanction.

Prior to 1978, the Secretary's only authority under the Act to impose fiscal sanctions on state education agencies ("SEAs") found to have misspent Title I education funds

was set forth in Section 146 of the Act, 20 U.S.C. § 241j; (1974) (repealed by 20 U.S.C. § 2836 (Supp. 1982), Pub. L. No. 95-561, Title 1, § 101(c), Nov. 1, 1978, 92 Stat. 2200.) That section authorized the Secretary to *discontinue* further payments to any state education agency he found had failed "to comply substantially with any assurance set forth in the application of the state approved" by the Secretary, but only until the state cured its noncompliance.[2] Nowhere in Section 146 or elsewhere did the pre-1978 Act authorize the Secretary to require a state to *repay* amounts found to have been misspent out of non-grant funds.

B. Authority for a repayment sanction cannot be read into the Act *sub silentio*.

The Department has argued that it has inherent authority to recover misspent funds from non-grant sources. (U.S. Br. at 15-23) The Department's argument fails for several reasons.

First, as a matter of law, the authority to require repayment of misspent grant funds from non-grant sources cannot be implied. As this Court in *Pennhurst State School* v. *Halderman*, 451 U.S. 1, 17 (1981) explained:

> The legitimacy of Congress' power to legislate under the spending power . . . rests on whether the State voluntarily and knowingly accepts the terms of the 'contract' [in return for federal funds]. . . .
>
> There can, of course, be no knowing acceptance if a State is unaware of the conditions or is unable to ascertain what is expected of it. Accordingly, if Congress intends to impose a condition on the grant of federal moneys, it must do so unambiguously.

(Footnote and citations omitted.)

Indeed, where Congress has chosen to authorize certain sanctions expressly, the courts have been reluctant to infer additional powers, particularly when the use of such

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[2] The statute arguably required disbursement of withheld funds once the noncompliance was cured.

powers might undermine the spirit of cooperative federalism that underlies programs such as Title I of the Education Act. Thus, in *Rothstein* v. *Wyman*, 467 F.2d 226 (2d Cir. 1972), *cert. denied*, 411 U.S. 921 (1973), the court refused to require a state to make retroactive payments to welfare recipients who had been underpaid by the state in part because "the only remedy [Congress] expressly contemplated was a prospective cut-off of funds." As the court explained:

> Congress has given no indication that it deems retroactive payments necessary to protect its interest, since the only remedy it expressly contemplated was a prospective cut-off of funds.
>
> Moreover, we cannot ignore the realities of the situation. The funds which were misspent are, as a practical matter, irretrievable. It would be unthinkable to order welfare recipients who received federal money under an illegal state program to return their checks. The reality is that the only means of redressing the harm to the federal treasury is to order the offending state to achieve *ex post facto* compliance through additional expenditure of its funds.
>
> That reality, however, invokes significant countervailing policies, namely, those behind the scheme of cooperative federalism alluded to earlier. Congress was clearly sensitive to the potential for serious strain in the federal structure inherent in a grant program of great magnitude and complexity. . . . Absent *explicit* directions from Congress to the contrary, we do not think that the federal interest in retroactively correcting the misuse of federal funds —the only federal policy applicable to this case—can by itself justify the significant increase in federal-state tensions which would result from a court order requiring the state to expend its funds against its will.

Id. at 235 (emphasis added).

Similarly, in *Wisconsin Department of Health and Social Services* v. *United States*, No. 80-C-234 (W.D. Wisc.

August 4, 1982), a decision the United States has decided not to appeal, the court ruled that where the Foods Stamps Act, 7 U.S.C. § 2011 *et seq.*, set forth some sanctions and the circumstances under which they could be imposed, authority for other sanctions could not be implied. *Id.*, slip op. at 9-10. Thus, where, as here, Congress authorized certain sanctions but failed to authorize the Secretary even in ambiguous terms, to require repayment of misspent funds, that power cannot be implied. *Pollard* v. *Bailey*, 87 U.S. (20 Wall.) 520, 527 (1874). *See also, National Railroad Passenger Corp.* v. *National Association of Railroad Passengers*, 414 U.S. 453, 458 (1974). ("A frequently stated principle of statutory construction is that when legislation expressly provides a particular remedy . . . , courts should not expand the coverage of the statute to subsume other remedies.")

Second, the Department ignores the fact that the pre-1978 Act specifically addressed the actions the Secretary could take in the event that he determined that Title I funds were not being spent substantially in accordance with the purpose or the provisions of the Act. It only authorized him to *discontinue* further payments until the noncompliance was cured. It did not authorize the Secretary to require *repayment of expended funds.* 20 U.S.C. § 241j.

In enacting the 1978 Amendments with specific authority to impose a repayment sanction, 20 U.S.C. § 2835, Pub. L. No. 95-561, 92 Stat. 2191, Congress did not, as the Department argues (U.S. Br. at 36), approve of authority it assumed the Department always had. Rather, Congress simply gave the Secretary authority he previously lacked. *Wisconsin Department of Health and Social Services* v. *United States, supra*, slip op. at 10. *Red Lion Broadcasting Co.* v. *FCC*, 395 U.S. 367, 381-82 (1969), relied upon by the Department (U.S. Br. at 36) is inapposite here. There, Congress, in explicit language, made clear that a statutory exception subsequently

adopted left intact the agency's construction of other provisions of the statute.

Finally, the government ignores the fact that Congress, when it chooses to do so, tailors the fiscal sanctions it authorizes to its particular program objectives. As we have noted, Congress originally authorized the Secretary only to withhold funds from states found to have misspent Title I education funds. 20 U.S.C. § 241j.[3] In 1978, it augmented the Secretary's authority to permit him to require repayment of misspent funds from non-federal sources. In 1981, Congress reversed its 1978 action, once again limiting the Secretary's remedies to the temporary discontinuance of payments and withholding of funds. 20 U.S.C. §§ 3803, 3872 (1982 Supp.). It is not surprising that Congress cut back the Secretary's authority in 1981 as part of its effort to "free the schools of unnecessary Federal supervision, direction, and control."

The history of the Comprehensive Employment and Training Act reveals a similar pattern. The original Act authorized the Secretary of Labor to discontinue "any further payments to [a] prime sponsor . . . [and to] notify such sponsor to return to him all or part of the *unexpended* sums paid under this chapter during the fiscal year" if, *inter alia*, the Secretary determines that the prime sponsor has failed "to carry out the purposes and provisions of this Act." Section 108(d), 87 Stat. 848 (emphasis added.) The Act also authorized the Secretary to "withhold funds otherwise payable under this chapter, but only in order to recover any amounts expended in the current or immediately prior fiscal year in violation of any provision of this chapter or any term or condition of assistance under this chapter." Section 602(b), 87 Stat. 878. Nowhere in Section 100(d), Section 602(b) or

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[3] The Secretary was also authorized to disapprove an application for funds where he was not satisfied that the state would satisfy the requirements of the Act. 20 U.S.C. § 241f.

elsewhere does the 1973 CETA Act authorize the Secretary of Labor to require a prime sponsor to repay amounts found to have been misspent out of non-CETA funds. Indeed, even the authority to withhold future funds from a prime sponsor is limited to "amounts expended in the current or immediately prior fiscal year."

In 1978, Congress recognized that the Secretary of Labor lacked authority to require repayment of misspent CETA funds when it amended the CETA Act to give the Secretary additional authority to impose fiscal sanctions on prime sponsors found to have misspent CETA funds. Section 816(d)(1) of the amended Act provides:

> [T]he Secretary shall have authority to terminate or suspend financial assistance in whole or in part and order such sanctions or corrective actions as are appropriate, *including the repayment of misspent funds from sources other than funds under this chapter* and the withholding of future funding.

29 U.S.C. § 818(d)(1) (1978) (emphasis added). The fact that Congress enacted this provision some four years after CETA had been in effect clearly indicates that Congress recognized that it had not, under the terms of the 1973 Act, authorized the Department of Labor to seek repayment of misspent funds from non-CETA sources.

In 1982, Congress revamped the CETA program and enacted the Jobs Training Partnership Act. Pub. L. No. 97-300, 96 Stat. 1322 (1982). Under the new provisions, the Secretary of Labor is authorized only to offset disallowed costs against other amounts due a recipient under the Act unless it is determined that "the misexpenditure of funds was due to willful disregard of the requirements of this Act, gross negligence, or failure to observe accepted standards of administration." Only in the latter case, is the Secretary authorized to require repayment from funds other than those received under the Act. Pub. L. No. 97-300, § 164(d) and (e), 29 U.S.C. § 1574(d) and (e).

Similar patterns exist in other grant programs. For example, under the Social Security Amendments of 1974, Pub. L. No. 93-647, 88 Stat. 2337, the Secretary of DHEW was authorized to either terminate payments or to reduce the amount payable to a state by three percent for each instance of noncompliance under Title XX. Section 2003(e)(2). Title XX was amended in 1981 to provide "[e]ach state shall repay to the United States amounts ultimately found not to have been expended in accordance with this title, or the Secretary may offset such amounts against any other amount to which the State is or may become entitled under this title." § 2006(b), 95 Stat. 867, 42 U.S.C. § 1397e(b).

The State and Local Fiscal Assistance Act of 1972 authorized the Secretary of the Treasury, upon learning of an instance of discrimination, to so inform the state and if, after a reasonable period of time, the state failed to correct the situation, refer the matter to the Attorney General or take action under Title VI of the Civil Rights Act of 1964. Pub. L. No. 92-512, § 122(b), 86 Stat. 932. The Attorney General was authorized to bring a civil action in district court. § 122(c). The provision was amended to give the Secretary the authority, upon a determination of noncompliance, to suspend payments, 31 U.S.C. § 1242(b)(3)(C), or to terminate payments, 31 U.S.C. § 1242(b)(3)(D). The State and Local Fiscal Assistance Amendments of 1976, Pub. L. No. 94-488, § 8(a), 90 Stat. 2350. These examples demonstrate that Congress was fully aware of the remedies available to it when both ESEA and CETA were enacted and that it selects only those sanctions it concludes are appropriate in a given context.

Congress also tailors sanctions authority to reflect the nature and gravity of erroneous expenditures by state and local governments. For instance, in the Welfare, Medicaid and Food Stamp areas, Congress from time to time has considered the imposition of repayment sanctions for erroneous payments made by sponsoring gov-

ernmental units. In considering such action, it has always been recognized that: (1) some errors in programs of this magnitude are inevitable; (2) a "zero-tolerance" (*i.e.*, total liability for *all errors*) is draconian and ultimately cost inefficient; (3) some leeway or "tolerance level" must be afforded to the administering governmental units; (4) sanctions should not be imposed without a "phase-in" period; and (5) if sanctions are to be used, an administrative machinery should be designed which offers the prospect of avoiding sanctions where the administering governmental unit could indicate that circumstances made "target levels" unattainable on any reasonable basis. *See, e.g.*, 7 U.S.C. § 2025 (1982 Supp.) (Food Stamps); 42 U.S.C. § 603(j) (1982 Supp.) (AFDC); *see also*, H. Rep. No. 95-345, 95th Cong., 2d Sess. *reprinted in* [1977] U.S. Code Cong. and Admin. News, p. 1704, 2289-2294.

The import of the sanctions provisions in these various programs is clear: authority to impose a particular sanction, especially the most drastic sanction possible, cannot be read into a statute governing an intergovernmental grant program.

II. THE 1978 ACT CANNOT BE RETROACTIVELY APPLIED.

In 1978, Congress recognized that the Secretary lacked authority to require repayment of misspent Title I funds when it amended the Act to give the Secretary authority to impose fiscal sanctions on SEAs found to have misspent Title I funds. Section 185(b) of the amended Act provides:

> Where, . . . the audit resolution process requires the repayment of Federal funds which were misspent or misapplied, the Secretary shall require the repayment of the amount of [such] funds . . . Such repayment may be made from funds derived from non-Federal sources or from Federal funds no accountability for which is required to the Federal Government.

20 U.S.C. § 2835(b) (1982 Supp.) The fact that Congress enacted this provision many years after the Act had been in effect clearly indicates that Congress recognized that it had not, under the terms of the pre-1978 Act, authorized the Department to seek repayment of misspent funds.

While the provision quoted above authorizes the Department to seek repayment of misspent funds disbursed after its enactment and implementation by regulation, it certainly cannot be given retroactive application to require repayment of funds disbursed and expended prior to the 1978 Amendments. New conditions and sanctions in a federal grant program should not be given retroactive application absent a clear Congressional intent to do so, as the Third Circuit concluded below. Relying on the principle set forth in *Pennhurst State School* v. *Halderman*, *supra*, "that the terms and conditions of a federal grant must be set forth clearly and unambiguously in the statute authorizing the grant," the court of appeals held that the statutory authority to require repayment of misspent funds could not be given retroactive effect to funds disbursed before the statute was enacted. (Pet. App. 14a)

As in *Rothstein*, the court below concluded that the retroactive application of a sanction such as asserted here would seriously undermine the spirit of cooperative federalism on which federal grant programs such as Title I of the Education Act are based and might discourage state and local government participation in such programs. (Pet. App. 12a-14a) *See also Solomon* v. *Califano*, 464 F. Supp. 1203 (D. Md. 1979).

The Third Circuit's refusal to give retroactive application to the repayment sanction at issue follows a well-established rule. As this Court stated in *Greene* v. *United States*, 376 U.S. 149, 160 (1964), "retrospective operation will not be given to a statute which interferes with antecedent rights . . . unless such be 'the unequivocal and inflexible import of the terms, and the manifest intention of the legislature,'" quoting *Union Pacific R.R.* v. *Laramie Stock Yards Co.*, 231 U.S. 190, 199 (1913); *see*

also Addisson v. *Holly Hill Fruit Products, Inc.*, 322 U.S. 607, 618 (1944). This Court recently reaffirmed "[t]he principle that statutes operate only prospectively [as distinguished from] judicial decisions [which] operate retrospectively." *United States* v. *Security Industrial Bank*, 51 U.S.L.W. 4007, 4009-10 (No. 81-184, 1982).

The Department seeks to avoid this basic principle by relying on *Bradley* v. *School Board of City of Richmond*, 416 U.S. 696 (1974). (U.S. Br. at 38) While *Bradley* and the cases that follow it enunciate the general principle that "a court is to apply the law in effect at the time it renders its decision, unless doing so would result in manifest injustice or there is statutory direction or legislative history to the contrary," *id.* at 711, this principle has little relevance to a federal grant program that defines the contract-like relationship between the federal government and a grantee, as stressed in both *Pennhurst* and the decision below.

More importantly, even if the principles of *Bradley* may be applied here, the repayment sanction should not be retroactively applied here because Congress did not intend to give it retroactive effect and because retroactive application would result in manifest injustice to New Jersey, Pennsylvania, and other grantees. In deciding whether retroactive application of a statute would result in manifest injustice, *Bradley* indicates that the following factors should be examined: the nature of the parties involved, the nature of their rights and the nature of the impact of the change in law upon those rights. *Bradley* v. *School Board of City of Richmond*, *supra*, 416 U.S. at 717. Examination of these factors in the present context compels the conclusion that retroactive application of the repayment sanction would be manifestly unjust.

Under Title I the federal government sought to involve state and local governments as partners in order "to meet the special education needs of educationally deprived children" in low-income areas across the country. Pub. L.

No. 874, Title II, § 205, *as added* by Pub. L. No. 89-10, Title I, § 2, 29 Stat. 27, 30 (1965) (*codified as amended* at 20 U.S.C. § 2734 (Supp. III 1979)). In doing so, Congress recognized the need to balance the federal government's objectives with traditional state and local control over education. *See* S. Rep. No. 146, 89th Cong., 1st Sess., *reprinted in* [1965] U.S. Code Cong. & Ad. News 1450. As the Court stressed in *Pennhurst*, a case decided after *Bradley*, a state or local government's voluntary and knowing acceptance of the terms of a federal grant depends upon Congress' unambiguous expression of the conditions imposed upon the grantee. *Pennhurst State School* v. *Halderman*, *supra*, 451 U.S. at 17.

All of the following factors bear on the fundamental unfairness of the harsh, many-years-after-the-fact sanctions urged here and in the CETA program:

1. At the time funds were received and spent by New Jersey and Pennsylvania, they, like all other grantee states, did not know that huge subsequent financial liabilities could be unleashed against them. Neither the statute nor the regulations said so. The states did not have to participate in the program and they would have wanted to weigh this potential liability in considering whether, and at what level, to participate.

2. The federal government was the lead partner in Title I programs and shares, or predominates, in any culpability for errors. It wrote the regulations and volumes of manuals, guides and instructions. Its agents were charged with responsibility to review the performance of SEAs and to correct erroneous actions in short order. Errors will be made in any program of this kind, but these are no more the fault of state and local governments than of the federal government, whose Congress created the program and whose agency supervised it. Yet the sanctions are all a one-way street; the states are to pay 100 cents for every misspent dollar. And the money is not to go to the intended beneficiaries but to the treasury of the federal partner in this operation.

3. The sanctions are wildly out of proportion to the alleged offenses. To take one example, many of the sanctions threatened in programs such as CETA relate to alleged errors in determining or documenting participant eligibility or in computing amounts of funds to be distributed in particular cases. Every social welfare program has errors of this kind. In considering the imposition of sanctions for such errors, however, Congress has recognized that it would cost more to attempt to eliminate all of the errors that inevitably occur in large, complex grant programs than the costs associated with those errors and that sanctions for such errors must be carefully tailored accordingly. Here, the Secretary, without statutory basis, has arrogated authority to himself that all errors must be punished, regardless of the cost of avoiding the errors.

4. The prospect that a state or local government may encounter difficulty in defeating sanctions even where federal supervising officials have expressly blessed, if not encouraged, adoption of the policies challenged, highlights the federal government's effort to shift the creative burden and the risks of mistakes to its state and local partners. Moreover, it makes the threshold legal question of controlling significance and the unfairness of reading this power into grant statutes even more pronounced.

5. Fundamental unfairness also stems from the timing of the imposition of sanctions. Had the federal government ascertained the errors at the time they were being made, the states could have taken corrective action without suffering any, or at the worst any significant, reduction in federal funds. The prospect of prompt corrective action lies at the heart of the scheme initially adopted by Congress and the refusal of Congress to provide any after-the-fact retroactive sanction powers in the pre-1978 Act. But the sanction power now asserted turns that scheme on its head. For the government is saying that it can impose sanctions now for errors committed as long

ago as 1970. There is nothing either state could have done to correct or limit the effect of any errors.

In *California* v. *Block*, 663 F.2d 955, 959 n.3 (9th Cir. 1981), the court concluded that it would be manifestly unjust to impose new sanctions permitting the collection of "money from erring state agencies" for acts that were performed prior to the enactment of stricter sanctions, relying on the principles of both *Pennhurst* and the decision reached below. The same conclusion should apply in this case. Having first secured the states' participation, it would be manifestly unjust for the federal government to retroactively apply a sanction that would require the states to draw on their limited fiscal resources to pay back misspent federal funds. No important federal policy would be furthered by such an action. It would not serve the purposes of the Title I program in any way; rather, it would only serve to enhance the federal treasury at the expense of the taxpayers of the two states. Accordingly, the fiscal sanctions contained in the 1978 Act should not be given retroactive application.

The Department's effort to apply the 1978 Act retroactively is further confounded by the Education Consolidation and Improvement Act of 1981, in which Congress continued the Title I program and specifically provided that the repayment sanction would no longer apply. 20 U.S.C. § 3803. Thus, Congress has returned to its pre-1978 approach by only authorizing the Secretary to discontinue payments and withhold future payments. *See* 28 U.S.C. § 3872, replacing 20 U.S.C. § 2836. By seeking to apply the provision in effect from 1978 to 1981, the Department suggests that it is free to choose that one version of the three statutory approaches Congress has adopted over the last ten years, and not that the Court must apply the provision in effect when the Court reaches its decision. But if *Bradley* has any bearing whatsoever here, it could only mean that the courts must recognize the fluidity of the law and follow the latest Congressional action. Surely the fact that Congress has changed its

approach twice demonstrates that the provision in effect at the time the states agreed to accept the funds is the one that should govern here. Only such an approach will ensure that state and local governments know what its federal government partner expects them to do.

III. THE DEPARTMENT'S REGULATIONS DO NOT AUTHORIZE IT TO IMPOSE A REPAYMENT SANCTION.

Even if the pre-1978 Act or the 1978 Amendments in terms authorized imposition of repayment sanctions under the current circumstances, the Department could not lawfully implement these sanctions under the terms of its regulations, for two related but independently dispositive reasons. First, the Department's regulations do not authorize imposition of the sanctions proposed in this case. Second, the Department cannot infer authority to create new sanction powers not prescribed in its regulations because that course is barred by the Administrative Procedure Act and well accepted principles of administrative law.

The Department's responsibility to follow its own regulations is beyond dispute. *See Service* v. *Dulles*, 354 U.S. 363, 372 (1957); *Rodway* v. *United States Department of Agriculture*, 168 U.S. App. D.C. 387, 514 F.2d 809, 814 (D.C. Cir. 1975); *Griffin* v. *Harris*, 571 F.2d 767, 772 (3d Cir. 1978); *United States* v. *Coleman*, 478 F.2d 1374, 1371 (9th Cir. 1973). At the relevant times, the regulations have dealt expressly with the topic of remedies for violations and have not set forth the sanctions that are sought here. The Administrative Procedure Act, 5 U.S.C. § 553, which applies here, 36 Fed. Reg. 2532 (1971), requires the adoption of formal rulemaking procedures, including notice, an opportunity to comment and *Federal Register* publication, prior to the adoption of agency regulations and the promulgation of a basis and purpose statement explaining significant provisions of the proposed regulations. There is no question

that when APA rulemaking procedures are applicable, action taken in derogation of them is void. *See e.g., Morton* v. *Ruiz*, 415 U.S. 199 (1974); *NLRB* v. *Wyman-Gordon*, 394 U.S. 759 (1969); *Texaco, Inc.* v. *FPC*, 412 F.2d 740 (3d Cir. 1969); *Kelly* v. *Department of Interior*, 339 F. Supp. 1095, 1102 (E.D. Cal. 1972).[4]

The Department thus confronted an obligation to set forth any claimed sanction powers in its regulations. There are twin reasons for that requirement. First, formal rulemaking procedures would help to assure a rational determination, on the basis of public rulemaking procedures and the record made therein, on the question of whether sanctions such as those here asserted advanced the purposes of the statute and constituted sound administrative implementation of it. For rulemaking procedures, if followed, could have satisfied the Department that use of the sanctions asserted here was undesirable. In any case, the sanctions could not be adopted until the Department had fully considered the necessity for such sanctions and had reached the opposite conclusion.

Second, if the Department had concluded that such powers were necessary, it would have been incumbent upon the Department explicitly to advise all who might be affected by the regulations of the full range of sanctions that could be imposed and the conditions under which each would be used. No state or local government was required to participate in the program; but all such governments considering that course were entitled to know, as a matter of equity as well as a matter of right under the legal authorities cited above, the financial risks that participation would entail. Only on that basis could they

[4] The cases stress not only the legal necessity of following rulemaking procedures, but the wisdom of doing so. The cases say that rulemaking procedures are "designed to assure fairness and mature consideration of rules of general application" and to "enable[] the agency promulgating the rule to educate itself before establishing rules and procedures which have a substantial impact on those regulated." Texaco, Inc. v. FPC, *supra*, at 744.

make responsible decisions. Having failed to promulgate regulations pursuant to either the pre-1978 Act or the 1978 Amendments which contain a repayment sanction, the Department is barred from imposing the sanction.

By not promulgating regulations implementing the sanctions power it claims to have had all along, the Department not only failed to resolve definitively the scope of its statutory powers but also to give any indication of the conditions under which it would impose retroactive fiscal sanctions. Thus, the Department simply assumed it had the power to require repayment of misspent funds and then applied it without considering the appropriateness of its use in particular cases. As this Court recently affirmed, however, an agency must provide compelling justification for the imposition of the most drastic sanction in its " 'arsenal of flexible enforcement powers.' " *Steadman* v. *SEC*, 451 U.S. 91, *rehearing denied*, 10 S. Ct. 2008 (1981), *aff'g.*, 603 F.2d 1126, 1139 (5th Cir. 1979). Moreover, Congress' expansion of the Department's sanctions authority in 1978 suggests that retroactive repayment sanctions ought not be automatically applied in all cases. Thus, the Department's failure to describe in advance the scope of its sanctions powers and the criteria that would govern the circumstances under which they would be exercised and its failure to justify the imposition of its most drastic remedy in this case violates both the *Steadman* test and Congressional intent.

IV. THE DEPARTMENT HAS NO POWER UNDER COMMON LAW TO SUSTAIN THIS SANCTION.

In urging that the common law and the Federal Claims Collection Act, 31 U.S.C. § 951 *et seq.* serve as independent bases for imposing sanctions apart from the statute (U.S. Br. at 24-31), the Department seriously misconceives and then misapplies this asserted source of authority. If the statute authorizes the imposition of these sanctions, the existence *vel non* of common law authority is irrelevant. But if the statute does *not* authorize imposition of sanctions of this sort, then the Department

begs the question in claiming authority under the common law and the Federal Claims Collection Act, for there exists no debt owing to the United States *to be enforced* under the common law.

The various flaws in the Department's analysis come down to these, each of which is independently dispositive of its common law contention:

1. The Department's analysis essentially rests on a line of cases which upheld the government's right to use the same common-law remedies available to a private person to enforce its contractual rights. (U.S. Br. at 15-16) But the precise question here is at what point and under what terms did Pennsylvania and New Jersey stand in the position of a party contractually indebted to the United States. They surely did not at the time federal funds were transmitted to them. Nor did some sort of debt obligation perforce arise when allegedly erroneous expenditures were made in the states' good faith efforts to administer these large and complex programs. That happens all the time, but a common law debt does not vest by virtue of that fact alone; none would participate if those were the rules.

Instead, the statute determines under what terms and when the actions of a state government can be analogized to a debt owing to the United States: it sets forth what activity is expected of states and just what sanctions may be employed by the United States. The point is that the common law provides measures to *enforce* some rights possessed by the United States; but something else must establish the right itself. Here the education statute does so, but not the one sought here.

2. Even if the education statute were viewed as something less than right-creating in the first instance, at the very least it undertakes to prescribe the full panoply of governmental remedies for alleged errors in implementing the program. This proceeding was commenced to impose sanctions under that statute. Under any accepted canon of statutory construction, the remedies section of

this statute would have to control in ascertaining the remedies possessed by this Department rather than some generalized and unarticulated "common law."

The withholding section has all of the earmarks of controlling force of law: it deals directly, expressly and thoroughly with the subject of remedies; it, rather than some notion of the common law, is used by the Department in implementing the statute; the statute, not the common law, is made known to all states; it was crafted relatively recently; and it, rather than the common law, served as the basis for promulgating the Department's regulations. It has been established for over a century that where a legislative body provides for liability coupled with a special statutory remedy, "that remedy, and that alone, must be employed." *Pollard* v. *Bailey*, 87 U.S. (20 Wall.) 520, 527 (1874). *See also National Railroad Passenger Corp.* v. *National Association of Railroad Passengers*, 414 U.S. 453, 458 (1974). Moreover, it comports with Section 9(b) of the Administrative Procedure Act, 5 U.S.C. § 558(b), which provides that no sanction may be imposed "except within jurisdiction delegated by the agency and as authorized by law."

The Department cannot escape the express list of statutory remedies by suggesting that the common law right of recovery survives the enactment of the Education Act. The pre-1978 Act and the 1978 Amendments provide for sanctions other than the repayment of past funding and, in any case, it requires more than the federal government's *post hoc* declaration to establish that a prescribed list of remedies means to embrace other but specified ones. If Congress intended that the Department have available to it all common law remedies, why did it not say so? Were the specified remedies mere surplusage in the pre-1978 Act? Why did the Congress feel constrained to add new powers in the 1978 Act if those were already available to the Department by virtue of common law without the amendment? And why did the Congress decide to return to the pre-1978 approach in 1981? These

questions suggest their own answer: the Department cannot advance its common law argument and leave in its wake any fair, or even plausible, meaning for the statute in its various forms.

3. The Department's own regulations bind it to employ only the sanctions and procedures prescribed in those regulations. *Service* v. *Dulles*, *supra*. The regulations incorporate the statute and rely *exclusively* upon the statutory sanction provisions. There is no mention of any authority claimed by the Department to impose sanctions in addition to those prescribed in the regulations or statutes but flowing instead from the "common law." Had the Department attempted in its regulations to arrogate to itself any common law powers, there would have been a substantial doubt as to the legality of such an effort, but there is no doubt that the Department has no such authority if it has not so much as undertaken to attempt to clothe itself with that authority in its regulations.

4. Whether or not the Department *could* set in motion a common law proceeding to impose retroactive sanctions, the present posture of the case indisputably is *not* that. A common law recoupment action would require initiation of a civil proceeding in a district court. This case simply involves an *administrative* disallowance proceeding regarding the Department's implementation of its asserted statutory sanction authority.

5. For reasons previously mentioned, the cases relied upon by the Department have nothing to do with ascertaining whether a debt exists in the first place. Its reliance on *West Virginia* v. *Secretary of Education*, 667 F.2d 417 (4th Cir. 1981), rests entirely on one sentence of unexplained dictum, which is overwhelmed by the thorough and thoughtful analysis of the same issue reaching the opposite conclusion in the decision below. *Mount Sinai Hospital of Greater Miami* v. *Weinberger*, 517 F.2d 329 (5th Cir. 1975), *cert. denied*, 425 U.S. 935 (1976) is inapposite because that decision rests in large part upon the special nature of that funding mechanism and the

legislative history of the statute there administered by HHS.

Most of the cases on which the Department relies for its recoupment argument involve the government's right to set-off monies owed it against future payments or claims against it. *See, e.g., Collins* v. *Donovan*, 661 F.2d 705 (8th Cir. 1981) (overpayment recovered by withholding future payments); *Jacquet* v. *Westerfield*, 569 F.2d 1339 (5th Cir. 1978) (erroneous assistance payment recouped by withholding current assistance); *Mount Sinai Hospital* v. *Weinberger, supra* (recoupment achieved against future federal funds). The only case where the government sought repayment was *United States* v. *Wurts*, 303 U.S. 414 (1938), a case commenced in district court to recover an erroneous tax refund. None of the cases cited by the government support the contentions it *must* advance here: that an agency has power to impose retroactive sanctions against a governmental cosponsor of an advance-funded grant program in the face of a statute and regulations (a) authorizing other sanctions, but (b) not authorizing imposition of the sanctions attempted to be invoked under the umbrella of the common law.

CONCLUSION

Amici curiae respectfully submit that the judgment of the Court of Appeals should be affirmed.

ROBERT N. SAYLER
JOHN E. HEINTZ
KAREN H. ROTHENBERG
JOAN E. DONOGHUE

COVINGTON & BURLING
1201 Pennsylvania Avenue, N.W.
P.O. Box 7566
Washington, D.C. 20044

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